MICHIGAN LEAGUE FOR PUBLIC POLICY

Testimony Presented to the House Tax Policy Committee

House Bill 4001
State Income Tax Reduction

Gilda Z. Jacobs, President/CEO

February 15, 2017

Good morning Chairman Tedder and members of the Tax Policy Committee. I am Gilda Jacobs, President and CEO of the Michigan League for Public Policy, a nonpartisan research and advocacy organization that promotes economic opportunity for all, regardless of race, place or income, and addresses poverty in a comprehensive manner. I thank you for the opportunity to testify this morning. We have several concerns with HB 4001, which would ratchet back the state income tax over the next 40 years.

This proposal will not create jobs or grow the economy as suggested and will disproportionately benefit the wealthiest taxpayers most. Instead, it will leave our state unable to invest in our schools, colleges and universities, communities, infrastructure, healthcare and public safety—the things that actually fuel economic growth.

Let's look at the facts which I hope you will weigh when considering this harmful legislation. While this appears to be a "drop in the bucket" when you look at the state budget as a whole, including federal dollars, the impact this legislation will have on state funds is significant. State income taxes make up about one-third of total state revenues, about one-fifth of state funds for schools, and 7 out of every 10 of our state's discretionary dollars.

The immediate impact of this legislation would be to eliminate $680 million from our state General Fund budget in fiscal year 2018 alone. This is equivalent to an about 7% across-the-board General Fund cut to all state departments, nearly half of state funding for colleges and universities, or total state General Fund dollars for around 10 state departments, including the funding for the Legislature. And the proposal would increase the amount of state revenue lost year after year, eliminating a revenue stream worth more than $9 billion once the income tax is fully repealed.

All of these budget decisions have a personal impact on the lives of Michigan residents. At a time when we are talking about reforming our criminal justice system, we wouldn't be able to provide returning citizens the support they need to be productive again. We also just started making investments so that our children can read proficiently. Taking money away would reverse that growth. These are the people who will one day be our doctors, lawyers, engineers, and skilled tradespeople; do we really think it's okay that we won't support them now so they can support us later? It would also impede our ability to put money into our Rainy Day Fund and save for the future or the next economic downturn, expecting our children to deal with budget cuts.

1223 TURNER STREET • SUITE G1 • LANSING, MICHIGAN 48906
P: 517.487.5436 • F: 517.371.4546 • WWW.MLPP.ORG
A UNITED WAY AGENCY

And your constituents agree with us. Recent polling shows that Michigan residents in your districts and around the state care more about the services they receive than they do about tax cuts. And they are highly concerned about the impact an income tax elimination could have without replacing those revenues.

If we think cutting off our ability to make these investments and pay for the things Michigan residents and job-providers rely on will grow the economy, we are fooling ourselves. All we need to do is look to other states that have recently gone through this to learn from their dismal outcomes. Take Kansas, for example. In 2012, Kansas enacted changes that eliminated taxes on a number of businesses and phased in income tax cuts. Instead of boosting the state economy, Kansas has been in a perpetual budget crisis, had to use gimmicks in order to patch budget holes, and had its credit downgraded several times. Schools have had to close weeks early, and due to raiding its road fund, the state went from being able to maintain its roads every 9 years to every 50 years. And some Republican Senators in Kansas are already scrambling to undo this mistake and repeal the tax cuts passed by their party's governor.

Take Mississippi—the state only recently started phasing in tax cuts and has already had to use reserves to patch a budget hole and now has a negative credit outlook which could impact its ability to deal with budget crises in the future.

Some have compared this proposal with how states like Texas and Florida have fared without ever having an income tax. That's like comparing apples with oranges. Unfortunately, Michigan does not have their warm weather or their oil, one of Texas' most significant revenue streams. Texas also taxes a number of services that we currently do not, and both states allow local option sales taxes.

On top of decimating our budget and our ability to attract and keep Michigan residents and businesses, a tax cut would disproportionately benefit Michigan's wealthiest taxpayers and contribute to rising income inequality. In the first year alone of an income tax reduction, taxpayers with low incomes, with an average income of $13,000, would get $16 back, middle-income taxpayers with an average income of $51,000 would receive $82, while those at the very top of the income scale, with an average income of over $1.5 million would receive $3,700.

Over 1 in 5 (22%) Michigan taxpayers would see no tax cut at all—including about 40% of the state's taxpayers who are struggling to get by (those making less than $22,000 per year). Two of every $3 in tax cuts would flow to Michigan's wealthiest 20% of taxpayers. The top 1% of earners, who make more than $484,000 per year, would take home 20% of the tax cut benefits.

On top of this, the proposal would ultimately eliminate the income tax. This will cause our already upside down tax system to get worse. In states that rely primarily on sales taxes, taxpayers with lower incomes pay a higher percentage of their incomes in state and local taxes than wealthier earners. Our state income tax allows our struggling taxpayers to offset their high sales and property taxes and level the playing field against higher-wage earners.

Phased-in deep tax cuts will only create major structural problems, weaken our ability to provide strong educational systems, safe drivable roads and bridges, and vibrant communities, and force our children and grandchildren to fix our mistakes. The current proposal would phase out taxes over 40 years so many of us won't even be alive by the elimination, and the rest of us will likely be retired elsewhere to avoid Michigan's winters. This allows all of you to avoid accountability for the problems these cuts will ultimately cause.

While Michigan is recovering from the Great Recession, we are not out of the woods yet. Our roads are still filled with potholes. Many of our schools are still struggling. And many of our Michigan residents still do not have safe, clean water to drink. Instead of tax cuts, we should be investing in the things Michigan residents and businesses need for a more secure future.

Taxes are all about collective impact. And while $82 for the average taxpayer might be a night out, we need to take a look at the deeper impact this will have on our state. Most families won't miss the $82—which isn't even enough to buy a coffee every week—but we will miss the teachers, vibrant communities and safe roads. The people of Michigan have told us as much. We just need to listen.

Thank you for your consideration.

Egads! Michigan wants to be like Kansas

michiganfuture.org/01/2017/egads-michigan-wants-to-be-like-kansas/

Lou Glazer 1/31/2017

As we have explored previously (see here, here and here), Kansas tried and failed to grow their economy through big tax cuts. In fact what they got was the exact opposite, arguably the worst state economic performance since the end of the Great Recession.

Despite the overwhelming evidence that cutting taxes doesn't grow state economies, it seems like the Michigan legislature is hellbent on replicating the failed Kansas playbook. This time by eliminating the state income tax. Not smart!

Let's quickly review what has happened in Kansas. This comes from a Bloomberg column by Barry Ritholtz, founder of Ritholtz Wealth Management. He writes:

> *In May 2012, he (Brownback) signed the bill into law. It initially lowered the top personal tax rate to 4.9 percent (it's now 4.6 percent) from 6.45 percent, but most importantly, it eliminated income tax on profits for owners of limited liability companies, subchapter S corporations and sole proprietorships.*
>
> *Give Brownback credit for passing the exact legislation he had promised.*
>
> *The results, however, haven't been very encouraging. Indeed, since the tax cuts were passed, almost nothing has gone as promised in Kansas. Revenue plunged and the state resorted to pulling money out of its rainy-day fund to plug the holes. A number of critical services, including for road maintenance and schools, were cut. The business climate has been poor, and the economy has lagged behind neighboring states as well as the rest of the country.*
>
> *… The math is simple: Tax cuts tend to reduce revenue, in Kansas' case much more than expected. To change people's behavior requires more substantial incentives than changing things by a few percentage points. The reduced revenue led to spending cuts that lowered quality of life. In response, rising numbers of people and companies have left the state.*

Ritzholtz details the economic underperformance of Kansas since the tax cuts:

- Kansas' gross state product fell behind the six-state region and the nation for the third straight year. (Kansas' gross state product grew at a faster rate when compared to the region and the nation in three of the five years before Brownback took office in 2011).
- Private industry wages in Kansas grew at a slower pace last year than they did in the region and the U.S. — as they did during the past five years.
- The number of private business establishments in Kansas trailed both the region and the nation for the last year, again continuing a five-year trend

Why did the experiment fail? As Ritzholtz explains: "Alas, reality trumps theory. As we have seen almost every time this thesis has been put into practice, it fails. The tax cuts don't magically kick the economy into higher gear and the government ends up short of money. Remember former President George W. Bush and his tax cuts? Same deal. … **The bottom line: The results from the economic laboratory known as Kansas are in. Supply side theory — and Kansans — lost.**" (Emphasis added.)

At the same time that Kansas was slashing taxes, California and Minnesota were raising theirs. In both cases, mainly higher income taxes on households with the highest incomes. What the tax cutters repeatedly tell us is the worse thing you can do to a state economy. Think again!

California arguably has had the best recovery of any state since the end of the Great Recession. The Washington Post reported:

> *California's economy grew by 4.1 percent in 2015, according to new numbers from the Bureau of Economic Analysis, tying it with Oregon for the fastest state growth of the year. That was up from 3.1 percent growth for the Golden State in 2014, which was near the top of the national pack.*
>
> *The Kansas economy, on the other hand, grew 0.2 percent in 2015. That's down from 1.2 percent in 2014, and below neighboring states such as Nebraska (2.1 percent) and Missouri (1.2 percent). Kansas ended the year with two consecutive quarters of negative growth — a shrinking economy. By a common definition of the term, the state entered 2016 in recession.*

And then there is Minnesota. It, as we detailed in our State Policies Matter report, has, by far, the strongest economy and the highest taxes in the Great Lakes. The lowest unemployment rate, the highest proportion of adults working, the highest per capita income and lowest poverty rate.

Michigan policymakers should have learned by now that cutting taxes is not effective in growing state economies from our own experience as well. We have been trying this playbook since the late 1990s. The result: Michigan for the first time ever is a low prosperity state with a strong Detroit Three. The last time the Detroit Three was thriving in 2000 Michigan had a per capita income at the national average. Today, having gone from a high tax state to a low tax state (see this Citizens Research Council report), Michigan is eleven percent below the national average. And there are roughly 400,000 fewer jobs in Michigan today than in 2000.

So no the states with the lowest taxes don't have the best economies. And definitely states without income taxes are not the most prosperous.

What correlates far better with high state prosperity is talent. The states with the highest education attainment.

As we have written frequently (see this 2010 post, this from 2014, and this from 2016) what matters is what you get from higher taxes. Yes there are benefits you get from taxes. The places with the strongest economies are those that combine high quality education systems and high quality of place that retains and attracts mobile talent. (And are also welcoming to all.) Both education and placemaking require public investments. These kind of public investments, paid for by our taxes, is the state policy playbook most likely to return Michigan to high prosperity, not more of the failed Michigan and Kansas tax cut after tax cut recipe.

Investing in infrastructure ... just words until you make the human connection

mlpp.org/investing-in-infrastructure-just-words-until-you-make-the-human-connection

From the First Tuesday newsletter
Sign up for the newsletter and e-news

I want to share with you a highly personal story about the death of my daughter Rachel in May of 2015 when the train she was riding from Philadelphia to New York derailed. It derailed because Amtrak (funded in part by our federal tax dollars) hadn't yet installed a proven emergency safety braking system.

This widely recognized technology would have stopped the train that was careening uncontrollably at high speed down the track. The technology to stop this accident from happening has been around for years. It just wasn't installed. As a result, Rachel and seven others lost their lives needlessly. Eight people died who had dreams and families and futures. They didn't have to die. It didn't have to happen. My 4-year-old grandson would still have his mommy if someone had "invested in infrastructure."

So why am I talking about this now so publicly? Because Michigan's lack of investment in our state's infrastructure in recent years is putting people's lives at risk, from a giant sinkhole damaging homes in Fraser to toxic water endangering an entire community in Flint.

And instead of offering solutions and increasing investment, some lawmakers want to undermine state services and infrastructure even more. There are proposals in Lansing right now to eliminate or reduce the state income tax. I've been around Lansing and budgets for long enough to know that **when taxes are cut it means cuts to schools, services, public safety and, yes, infrastructure**—pipes carrying water to our homes, workplaces and hospitals; roads and bridges that are supposed to carry us safely to school and work and back home at the end of the day; school buildings that house our children for more than seven hours a day and more.

And bad things can and will happen unless we stop this thinking that all taxes are bad. Taxes protect our very lives, our children and our communities. They are the price for living in a democratic society where we must share the responsibility of people looking out for their neighbors, their neighbors' children and parents.

We know what happened in Flint when a decision to save money by switching the city's water source, and another appalling decision to save a few thousand dollars by not treating the pipes with a chemical to prevent lead from leaching into the water, exposed thousands, mostly kids and seniors, to toxic lead. **The damage of these decisions will be felt for decades to come.**

We know what happened in Flint when state health officials failed to test Flint's water for Legionella or heed warnings of an outbreak as Legionnaires' disease took the lives of a dozen people and sickened nearly 100, and pneumonia killed 177 Genesee County residents in 2014 and 2015.

And we know that what happened in Flint could happen again anywhere in Michigan and that other failing infrastructure is jeopardizing residents as we speak.

Please join me in letting our Legislature know that we can't cut our way to prosperity—**that our tax decisions can indeed be life-and-death decisions.** I implore our elected officials to put a human context to their actions moving forward because there are real people behind all those budget numbers and decisions. **Perhaps my daughter's tragic death will not have been in vain if positive change can come as a result. Whether it's at the state or federal level, government's deadly mistakes must be resolved not repeated.** Please tell your lawmakers to be responsible and think of the human beings that are behind their decisions. Tell them not to cut taxes or state services and instead use those dollars to invest in the very things that will provide a safer, better life for us all.

— *Gilda Z. Jacobs*

- Home
- About
- Kids Count
- Policy
- Resources
- Take Action
- Events
- Blog

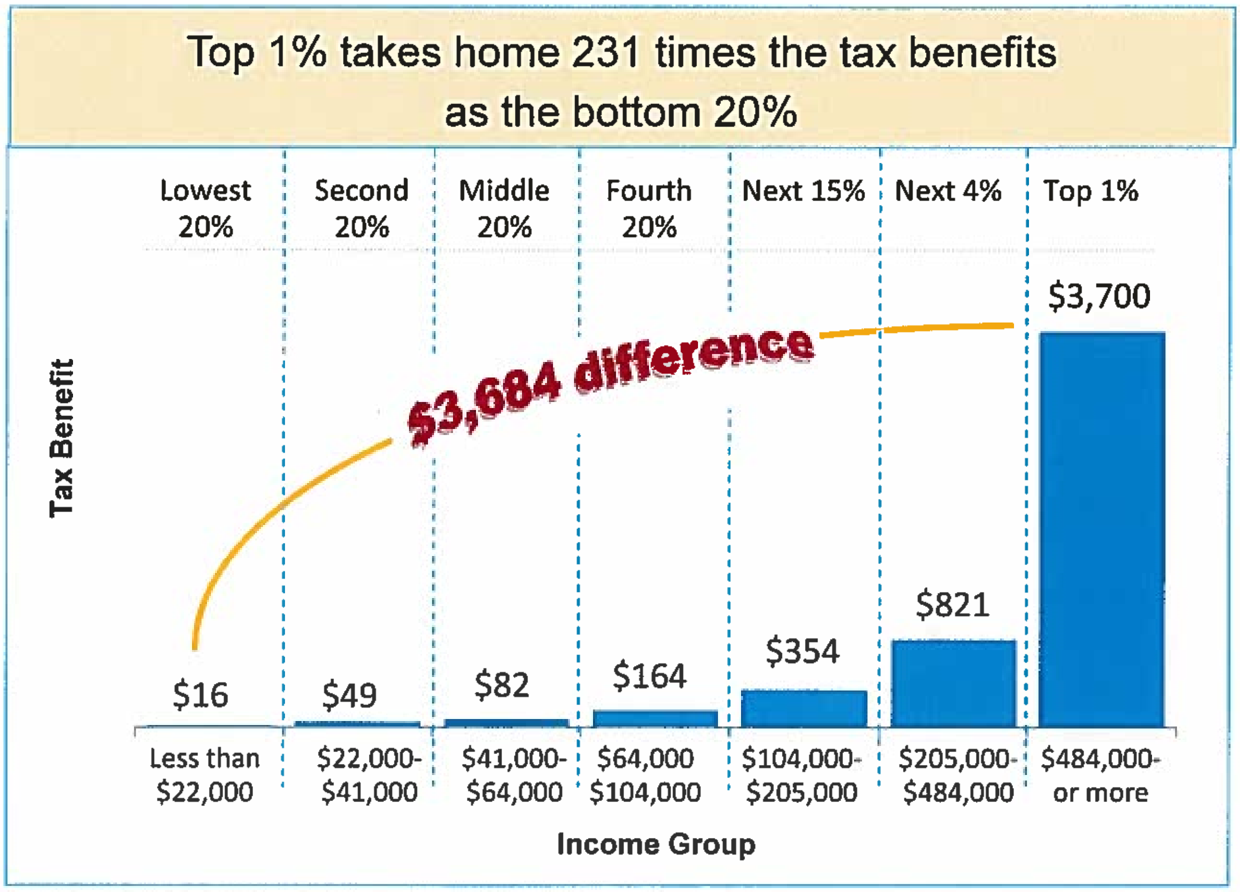
Michigan League for Public Policy
1223 Turner Street STE G1
Lansing, MI 48906-4369
Phone: (517) 487-5436 Fax: (517) 371-4546

February 2017

MICHIGAN LEAGUE FOR PUBLIC POLICY

INSTITUTE ON TAXATION AND ECONOMIC POLICY

Who Benefits: Income tax rate cut to 3.9% helps wealthy most



Source: Institute on Taxation and Economic Policy, February 2017

1223 TURNER STREET • SUITE G1 • LANSING, MICHIGAN 48906
P: 517.487.5436 • F: 517.371.4546 • WWW.MLPP.ORG
A UNITED WAY AGENCY

February 2017

MICHIGAN LEAGUE FOR PUBLIC POLICY

INSTITUTE ON TAXATION AND ECONOMIC POLICY

Who Benefits: Income tax rate cut to 3.9% helps wealthy most

Income of $22,000 or less

The bottom 20% would receive

$16

Enough for takeout pizza

Income of $41,000—$64,000

Middle 20% would receive

$82

Dinner for 2 at a nice restaurant

Income of $484,000+

The top 1% would receive

$3,700

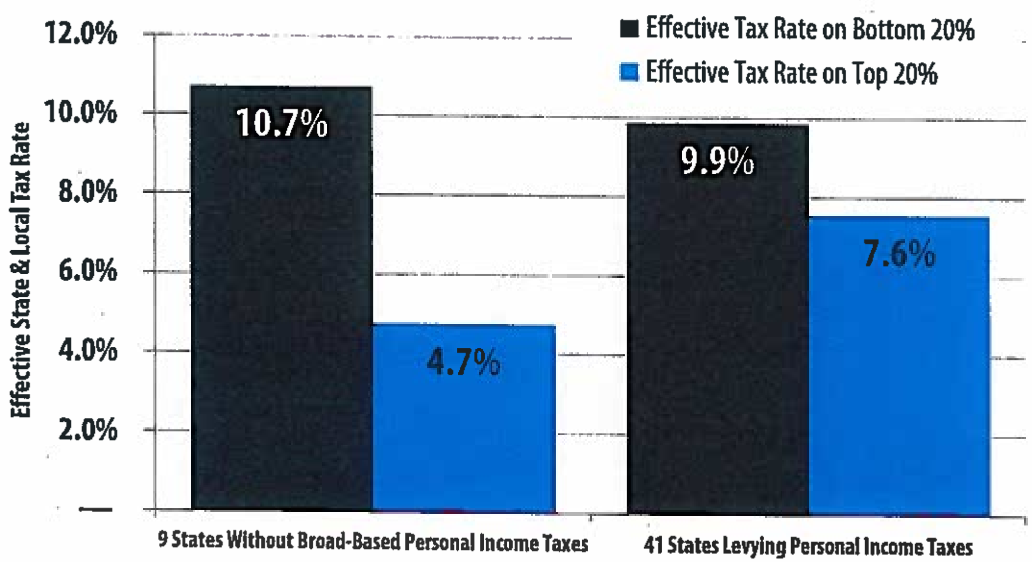
Flight to Paris, sights and dinner

Source: Institute on Taxation and Economic Policy, February 2017

1223 TURNER STREET • SUITE G1 • LANSING, MICHIGAN 48906
P: 517.487.5436 • F: 517.371.4546 • WWW.MLPP.ORG
A UNITED WAY AGENCY

4

States without Personal Income Taxes Tend to Levy Higher Taxes on Low-Income People



Source: Institute on Taxation and Economic Policy (ITEP)

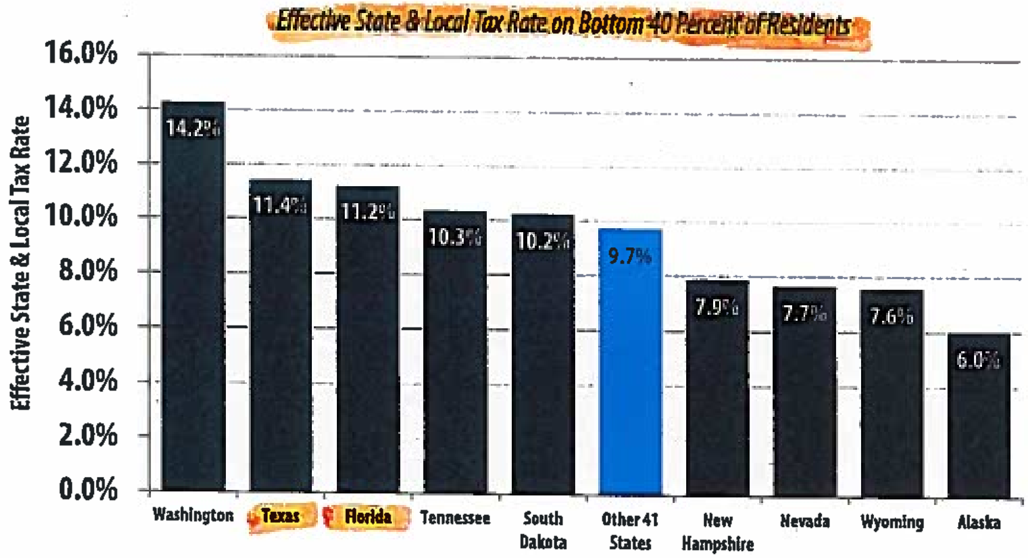
Not levying a personal income tax requires tradeoffs that are often detrimental to tax fairness

It is a common misconception that states without personal income taxes are "low tax." In reality, to compensate for lack of income tax revenues these state governments often rely more heavily on sales and excise taxes that disproportionately impact lower-income families. As a result, while the nine states without broad-based personal income taxes are universally "low tax" for households earning large incomes, these states tend to be higher tax for the poor.

Note: The nine states without broad-based personal income taxes are Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington, and Wyoming.

5

Low- and Moderate-Income Families Usually Face Above-Average Tax Rates in States without Personal Income Taxes



Source: Institute on Taxation and Economic Policy (ITEP)

States without personal income taxes are not necessarily "low tax" for everyone

Five of the nine states without broad-based personal income taxes require their low- and moderate-income taxpayers (those in the bottom 40 percent of the income distribution) to pay more than 10 percent of their income in state and local taxes each year. Among states that levy personal income taxes, the average effective tax rate for this group is 9.7 percent.

Of the four non-income-tax states with lower tax rates on low- and moderate-income families, three (Alaska, Nevada, and Wyoming) have sizeable mining and tourism sectors that allow them to collect significant tax revenues from non-residents. Additionally, two of these four states (Alaska and New Hampshire) lack a statewide general sales tax. States that compensate for the lack of a personal income tax by levying higher taxes on consumption tend to be "high tax" states for low- and moderate-income families.